

Chapter 3.

Challenges and Opportunities

Should the Tobacco Program Be Abolished? No.

During our deliberations, the question was raised about whether the tobacco program should simply be abolished in favor of contracting. But the Commission often heard that eliminating the tobacco program would create major hardships for most tobacco farms, particularly small family-run operations, and at the same time fail to serve public health goals. Overall, U.S. tobacco production and sales would probably increase if the program were eliminated, but prices would drop considerably. Many farmers would not be able to make up for the price cuts through increased sales.

Based on an analysis of historical data and existing circumstances, tobacco economists and researchers have developed estimates of how much U.S. leaf prices would drop and sales would increase if the tobacco program were eliminated. Studies suggest that a 25-percent reduction in price would increase overall U.S. tobacco leaf sales by about 36 to 62 percent, although the most recent study supports the lower figure. A 1999 study by agricultural economists and tobacco specialists Blake Brown, William Snell and Kelly Tiller calculated that the end of the tobacco program would reduce burley prices by more than 20 percent, but burley sales would increase by only 13 to 16 percent. They projected that flue-cured prices would drop by about 27 percent, but that flue-cured sales would increase by 84 to 89 percent.

However, the Commission also heard that the flue-cured sales figures are too

high because of the likelihood that offsetting price reductions and other adjustments would occur in competitor countries.

These calculations suggest that burley growers, as a whole, will suffer more from the end of the tobacco program because the overall increased demand for burley will not compensate for the price drop. Note that there are many more burley growers than flue-cured growers in this country.

It is also likely that many flue-cured growers cannot expand their production sufficiently or at a low enough cost to make up for reduced flue-cured prices, and many small-scale flue-cured growers will not be able to compete successfully against larger farms with lower production costs.

The end of the tobacco support program would also prompt a substantial shift of income and profits from current U.S. tobacco growers and quota owners to the U.S. cigarette manufacturers and dealers. Brown, Snell and Tiller calculate that the loss of quota value alone caused by the end of the tobacco program would transfer over \$500 million per year in income from quota owners to the cigarette manufacturers. Based on the cost savings caused by the declines in U.S. and foreign tobacco leaf prices, others have estimated that the end of the tobacco program would transfer \$800 million or more per year to the cigarette companies from tobacco farmers.

We note too that as discussed in the preceding Findings chapter, the tobacco program contains provisions that are consistent with public health goals.

The Commission therefore concludes that eliminating the U.S. tobacco program would not be beneficial to tobacco growers, their communities or public health. Instead, we contend that

significant changes must be made to current federal tobacco policy — changes that will eliminate artificial production costs caused by the quota system and allow producers who want to quit tobacco production to do so. A new tobacco policy should treat quota owners and tobacco growers who have depended on the current system fairly, while protecting public health, and provide remaining producers an opportunity to survive and prosper.

Opportunities to Assist Tobacco Farmers and their Communities

At our public hearings and in written comments, we heard from a broad spectrum of agricultural, health, economic and community representatives. They described existing and potential initiatives that could play key roles in ensuring both the short- and long-term viability of tobacco-growing communities and regions, several of which are outlined here.

Agricultural and economic development strategies. The Commission heard from numerous experts, local officials and farmers concerning the issues of agricultural and economic development in tobacco-dependent communities. We reviewed a 1995 survey of tobacco farmers, in which the majority indicated an interest in trying on-farm non-tobacco ventures to supplement tobacco income, and learned from testimony at our hearings that, some six years later, the interest of tobacco farmers in alternative forms of income is still high. Because of the recent, sharp declines in demand for tobacco leaf and subsequent declines in tobacco-growing income, new agricultural and off-farm income options for existing farmers have become critically important.

A few tobacco-growing states are assisting tobacco farmers and their communities with funds that the states received as a result of the Master Settlement Agreement signed by states and cigarette manufacturers. Tobacco quota owners and growers are also receiving some monies over a 12-year period from cigarette manufacturers. But those “Phase II” payments are tied to cigarettes sales, which appear to be on a steady decline. Thus, the payments represent an uncertain source of income at best for future investments. What is more, financial assistance is only part of the solution. Planning and technical assistance are also necessary to help small communities diversify their economic base.

As USDA recently reported, a number of counties — primarily in Kentucky, North Carolina and Virginia — that depend on tobacco for a significant share of local income have generated relatively few economic alternatives to tobacco. Despite the need for planning and technical assistance to help such counties and communities, there is no comprehensive economic development strategy for the tobacco-growing region, let alone one that addresses the diverse needs of each tobacco-growing community.

We learned of several agricultural and economic development and diversification projects and programs that may well help improve the longer term economic prospects of many tobacco farmers and tobacco-farming communities, as discussed below.

On-farm diversification. Many tobacco growers already raise crops other than tobacco or have other sources of farm income to supplement their tobacco revenues. However, increasing the amount of non-tobacco

farm income, we were told, must entail more than simply increasing production of supplementary crops or livestock. Existing markets may not be able to absorb significant growth in non-tobacco agricultural products or could do so only through price cuts that would reduce farmers' incomes.

Thus, initiatives to augment farm income from non-tobacco crops should identify or develop new markets and ensure that tobacco farmers have access to them. Some tobacco farmers are focusing on "niche" markets for potentially high-value crops such as organic produce, medicinal herbs and specialty mushrooms.

A number of agricultural diversification and development efforts may help guide tobacco-dependent farmers and their communities. Land-grant universities, extension services, state departments of agriculture, non-profit foundations and tobacco farm organizations are assisting farmers in identifying and adopting viable alternatives that can provide high (*and stable*) returns per acre. And several USDA, Appalachian Regional Commission and Small Business Administration programs have funded new initiatives in recent years for tobacco diversification.

Entrepreneurship. New, locally owned businesses — both on and off the farm — that create jobs and increase local wealth are an option for some communities. Success depends in large part, the Commission heard, on a community's willingness and ability within its own particular circumstances to provide the infrastructure, including capital and technical assistance, that is needed to attract and support entrepreneurs.

Tobacco-growing communities may choose to strengthen their ties to local economic development agencies such as multi-county development districts, county industrial authorities or local chambers of commerce. These organizations work on a daily basis to bring new businesses and jobs to the towns and counties they serve. And while the majority of them focus on finding medium- and large-scale industries to locate in their areas, many also can work with a specific community to help it identify its particular strengths and look for new opportunities.

Finding the money. Many farmers who wish to pursue non-tobacco income, both on the farm and off, may face difficulties in obtaining the funds needed to finance new ventures. We heard that studies of rural capital markets indicate such financing exists, but that small tobacco farmers seeking financing in markets they are unfamiliar with may well be viewed as high-risk borrowers.

Avenues to explore include Development Venture Capital (DVC) funds, which several rural communities have launched to attract new sources of equity financing. Like traditional venture capital funds, DVCs seek a strong return on investments, but they also are aimed at ensuring social benefits to the communities.

Micro-credit funding, which provides loans for small new economic ventures, is another possible source of financing new businesses. These funds are typically offered through non-profit organizations supported by government and foundation grants.

We also note that some capital will be available to tobacco quota owners and growers as a result of our

recommendation for a Tobacco Equity Reduction Program (see *TERP, Chapters 4 and 5*).

Community access to resources. While numerous government and non-profit programs offer technical assistance and resources that could help farmers and their communities pursue new economic strategies, people in rural areas dominated by small farms are often not familiar with nor do they typically possess the knowledge of how to “capture” these resources. A critical need, the Commission found, was to provide targeted technical assistance directly to such communities to help them shape the direction they want to take and avail themselves of the resources necessary to take the first steps.

“First, agriculture is considered a fundamental part of [tobacco-growing] communities, and the communities want it to remain that way. Second, the work of this Commission must reflect the diversity of these communities. One size does not fit all. Innovative, county-based and county-involved approaches are the best hope we have for our tobacco-dependent communities.”

Chris Beacham,
Research Director, North Carolina
Economic Development Center

Federal agency coordination. The Commission has learned of several efforts by the federal government to coordinate federal resources across regions that are dealing with special economic development challenges. These efforts might serve as models for similar work in tobacco-dependent communities. They include the President’s Economic Adjustment Initiative for the Pacific Northwest and Northern California, which provides funding and technical assistance to timber-dependent communities in the Pacific Northwest; the Delta Regional Authority, representing the multi-state Lower Mississippi Delta region; and the President’s Interagency Task Force on the Economic Development of the Southwest Border, which covers 56 counties in California, Arizona, New Mexico and Texas.

Developing new uses of tobacco that do not harm the public health. For decades, the use of tobacco has been associated with causing death and disease. However, the Commission heard about various alternative uses of tobacco other than for smoking or other consumption. As examples, researchers and bioengineering entrepreneurs have begun to use tobacco plants as hosts for bioengineering processes that may produce new antibiotics, vaccines, cancer treatments, other medicines, blood substitutes and even biodegradable plastics and industrial enzymes and solvents.

In China, scientists are now using tobacco as a culture medium for research on the foot and mouth disease that is causing havoc in England and elsewhere. And researchers are exploring the use of genetically engineered tobacco plants to clean up

contaminated areas just by growing them in the contaminated dirt.

In Virginia, some tobacco farmers have formed their own company to work with the biotechnology industry on uses for transgenic tobacco. It appears there is merit in encouraging other tobacco farmers to explore similar ventures. Growing tobacco for non-harmful uses may be an area where public health organizations, tobacco farmers, the biotechnology industry and government agencies such as USDA, FDA and the National Institutes of Health can work together. The goals would be to develop and administer a coordinated plan to protect and benefit both the public health and tobacco-growing communities.

In addition, we noted in our preliminary report that numerous technologies have had and will have impacts on the way tobacco is grown, processed and eventually manufactured. Some of those technologies remove toxins from and reduce the level of nicotine in tobacco. Others involve improving per-acre yields of tobacco and controlling for plant diseases.

The Commission believes that such technological developments and others may, if handled carefully, have positive economic impacts on U.S. tobacco growers and contribute to the public health goals. We agree that through education and training in new technologies, U.S. tobacco growers have an opportunity to improve their competitive position at home and abroad and contribute to public health goals.